

FILED 08 '95 15152 BUSINESS COUNCIL OF THE LEGISLATURE

DEPARTMENTAL BILL # 98

1993 ARTICLE VII # 16

MEMORANDUM IN SUPPORT

SENATE
1845ASSEMBLY
3145

A BUDGET BILL submitted by the Governor
in accordance with Article VII of the Constitution

AN ACT to amend the tax law and the criminal
procedure law, in relation to the
prepayment of tax on sales of cigarettes
under article 28 of such law and
pursuant to the authority of article 28
thereof

Purpose:

To enhance sales tax compliance by requiring the prepayment of
sales and compensating use taxes on cigarettes.

SUMMARY of Provisions:

Section 3 of this bill amends Article 28 of the Tax Law by adding
a new section 1103 to require cigarette tax agents to prepay tax
imposed by such section 1103 on account of the sales and use
taxes imposed by and pursuant to Articles 28 and 29 of such law.
Subdivision (a) of such section imposes the prepaid tax and
provides that such tax shall be paid at the same time and in the
same manner as the cigarette taxes imposed pursuant to Article 20
of such law, including the bonding provisions thereof. The
prepaid tax will generally be administered, collected, deposited
and disposed of in the same manner as the sales and use taxes.
This section also provides that the prepaid tax will be collected
only once.

Section 1 of the bill conforms the existing deposit and
disposition of revenue provision in section 171-a(1) of the Tax
Law to the deposit and disposition provisions of new section
1103.

Sections 2 and 4 of the bill amend Tax Law sections 1101 (b) and
1111 (d), respectively, to conform the provisions of the Article
28 definition of retail sale and the schedule of sales tax
required to be collected on retail sales of cigarettes, to permit
the prepayment of sales tax on such sales of cigarettes.

Section 5 of the bill amends Tax Law section 1111 to establish a
prepayment rate of 7 percent under new section 1103 and provide
for determination of the base retail price for purposes of
calculating the prepaid tax.

Sections 6 and 7 of the bill amend Tax Law sections 1115 and
1116(b) to limit the exemptions applicable to the prepaid tax.

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Section 8 of the bill amends the Tax Law by adding a new section 1131 to provide for refunds and credits with respect to the prepaid tax in conjunction with the payment of sales and compensating use taxes, as well as the export or destruction of cigarettes to which stamps evidencing payment of the tax have been affixed.

Section 9 of the bill makes a conforming reference in Tax Law section 1132(c) to new subdivision (k) of section 1132 as added by section 10 of the bill. Section 9 also makes technical corrections to section 1132(c).

Section 10 of the bill amends Tax Law section 1132 to provide that no one may purchase cigarettes unless the prepaid tax has been paid and passed through, and make a person who has not borne the burden of the tax liable. This section also provides that except for the retail sale, the seller must give a certificate to the purchaser at the time of delivery which provides that: (a) if the seller is an agent, the agent has paid the tax; or, (b) if the seller is not an agent, the seller is passing through the tax assumed by such seller. If such certification is not given, the purchaser bears the burden of proving that such tax has been paid.

Section 11 of the bill amends Tax Law section 1134(a)(1) to require persons selling cigarettes to file a certificate of registration.

Section 12 of the bill amends Tax Law section 1135(a) to provide that the Commissioner of Taxation and Finance may require persons selling large quantities of cigarettes to keep records of purchases and sales.

Section 13 of the bill amends Tax Law section 1136(a) to provide that the returns of sellers of cigarettes shall show the amount of prepaid tax assumed and passed through, and such other information as the Commissioner may require.

Section 14 of the bill amends Tax Law section 1138(a)(3) to provide for the assessment of the penalty which may be imposed pursuant to section 16 of the bill.

Section 15 of the bill amends Tax Law section 1142 to provide for joint administration, in whole or in part, of the prepaid tax and the tax imposed pursuant to Article 20 of the Tax Law.

Sections 16 and 17 of the bill amend Tax Law sections 1145(a)(1) and 1145(a)(3)(i), respectively, to provide for the imposition of penalties on persons required to collect the tax who willfully and knowingly have in their possession and control cigarettes on which the prepaid tax has not been paid and passed through, or

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sell cigarettes without possessing a certificate of authority.

Section 18 of the bill amends Tax Law section 1145(e) to provide for personal liability for responsible individuals of businesses which fail to pay the tax imposed by new section 1103 for the amount of tax not paid.

Section 19 of the bill amends Tax Law section 1817(1) to impose criminal liability on a person who willfully fails to pay tax or file a return with respect to the purchase or use of cigarettes, in the same manner as currently exists with respect to failure to pay tax or file a return relating to automotive fuel.

Section 20 of the bill amends the Tax Law by adding a new section 1817(q) to impose criminal liability on the owner of a business selling cigarettes at retail who willfully and knowingly has in such owner's custody or possession cigarettes upon which the tax has not been paid and passed through. The offense is a misdemeanor unless the amount of cigarettes in question is 20,000 or more, in which event the offense is a class B felony. New subdivision (r) is also added to section 1817 to impose criminal sanctions regarding counterfeit stamps evidencing payment of the prepaid tax, or purchasing or tendering such stamps or devices to counterfeit stamps. Subdivision (r) is modeled on section 1814(i) of the Tax Law providing similar sanctions with respect to Article 20 cigarette excise tax stamps.

Section 21 of the bill amends Tax Law section 1817(s) as relettered by section 20 of the bill, to add a necessary cross-reference to section 1103 added by bill section 2.

Sections 22 and 23 amend section 1.20(34)(q) of the Criminal Procedure Law and sections 24 and 25 amend section 2.20(4)(a) of the Criminal Procedure Law to provide that Department employees who are designated police officers and peace officers, respectively, are authorized to enforce sales and compensating use taxes with respect to cigarettes, in the same manner that such officers are currently authorized to enforce such taxes on automotive fuel, which is subject to a prepaid tax similar to the prepaid tax on cigarettes added by this bill.

In order to ensure the collection of the prepaid tax with respect to cigarettes in the distribution process in the state on the date the prepaid tax takes effect, bill section 26 imposes a floor tax on cigarettes possessed in the state for sale other than at retail on such date.

Section 27 of the bill is the severability provision.

Section 28 provides that the act takes effect immediately except that sections 1 through 22 and 24 shall take effect September 1, 1995. In addition, the amendments to the Criminal Procedure Law

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by sections 22 and 24 shall be subject to the expiration and reversion provisions of Chapter 808 of the Laws of 1993, and upon such date, the provisions of sections 23 and 25 of the bill shall take effect.

Existing Law:

Existing law does not provide for a prepayment of sales tax on cigarettes. As with other types of tangible personal property, sales tax relating to cigarettes is collected on the retail sale.

Statement in support:

The retail cigarette trade exhibits traits often associated with sales tax compliance problems. Tens of thousands of retail businesses sell cigarettes in New York State, many on a cash basis. Nearly 40 percent of all cigarette sales are made by small and medium sized businesses.

Unlike most other goods and services, the State regulates the importation and wholesale distribution of cigarettes. The State authorizes approximately 168 cigarette stamping agents (agents) to import unstamped cigarettes into New York. They must affix cigarette excise tax stamps to each pack they distribute. Among cigarette distributors, only licensed agents may legally possess unstamped cigarettes. Once stamped, agents distribute the cigarettes to licensed wholesalers, chain stores or retailers. At each level of distribution, State law specifies minimum sale prices based on required price markups. In no case may retailers sell below the mandated minimum price.

Despite these controls, representatives from the industry and Department of Taxation and Finance report sales tax compliance problems at the retail level.

This proposed change would require prepayment by licensed cigarette stamping agents of a significant portion of the sales tax due on cigarettes. Agents would make the prepayment when they purchase State excise tax stamps, and (through a process now used for the motor fuel prepayment system) would pass the amount of prepaid tax down the distribution chain - ultimately to the retail vendor. Vendors would have to account separately for these transactions.

Retailers would continue to collect sales tax on retail sales of cigarettes in the same manner as they do now. However, under this bill, they would take a credit on their sales tax returns for the amount of prepaid tax paid to their suppliers. The retailer would only remit to the State the difference between the prepaid tax paid on its purchases and the actual amount of tax collected on the retail sale. If the amount of tax prepaid exceeded the amount of tax actually collected on the retail sale,

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the retailer would qualify for a credit or a refund.

This change would provide tax enforcement benefits because moving the collection of the tax to the agent level would reduce the number of businesses responsible for a significant portion of the tax to a small, easily identifiable group (approximately 165 agents versus tens of thousands of retail vendors). This would result in a more narrowly focused and easily managed compliance program.

Under the bill, agents would pay a large portion of the sales tax prior to distributing the cigarettes, and would create the documentation certifying payment of the tax. Therefore, the bill would significantly diminish opportunities for retailers to underpay or avoid tax. Moreover, the tax prepayment would ensure that if a retail business became insolvent, the State would have already received a large portion of the sales tax due on the retail sale of cigarettes.

Furthermore, to obtain credit for prepaid tax on purchases, a vendor would need to report to the Department the amount of prepaid tax on purchases. This would require that records of purchases and sales be carefully maintained. Thus, the program should yield an improvement in recordkeeping and reporting by vendors.

A floor tax is necessary to ensure that current inventory in the hands of agents and wholesaler dealers (but not pure retailers) is not sold after the effective date without payment of tax.

The bill will produce an additional continuing source of revenues for State and local governments through increased compliance.

Budget Implications:

This bill will result in additional net State sales and use tax collections of approximately \$9 million in 1995-96. These receipts are reflected in the Financial Plan; thus, enactment of this bill is necessary to implement the 1995-96 Executive Budget.

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RJ REYNOLDS

ID:

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TRANSMIT CONFIRMATION REPORT

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